

Identifying and Ranking the Audit Problems of Small Firms from the Perspective of the Certified Public Accountants

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ABSTRACT

The present paper aims at investigating and ranking the audit problems of small auditing firms from the certified public accountants' point of view. The sample is composed of 90 individuals selected by using simple random method. The required data is collected through a questionnaire including 27 questions. The audit problems are identified by using the existing literature and interviewing with some members of certified public accountants. Based on the data gathered from the questionnaires, the problems of the small audit firms are ranked by statistical methods and TOPSIS approach. The findings reveal that all respondents consider the whole problems significant. From the perspective of the respondents, the weakness of the internal control system is the major weakness; while lower financial and social knowledge of the small firms' directors is problem with the least significance.

KEYWORDS: Audit Problems, Small Firms, Certified Public Accountants, TOPSIS Technique

1-INTRODUCTION

There is a money-making commerce around the world which is a part of Asian culture and the small firms have the ability to conduct more operations (Crick. et al., 1995) Today, the content and qualitative changes occurred in the global markets and the specific approach which considers the customer orientation developed the industrial structure of the manufacturers through variation of small and medium firms (Dimen. 2004) Additionally, the small and medium firms can make themselves consistent with the quick variations of the environment and quickly react to the economic and political factors (UNCTAD, 2000). During the recent changes and the complexity of the managerial and decision-making processes, the need to make immediate and essential decisions has dominated the significance of the small and medium firms (UNCTAD, 2000). The scholars also found that the small and medium firms gain more return than the big ones (Christopher et al, 1999; Drew E et al 2003). Based on the difference in the comprehensive definition of the small firms in different countries, we have selected the entities with less than 50 workers as the small firms. This description is consistent with the definition of the ministry of industry and central bank of Iran which considers the occupation as the only factor of classifying small firms (WWW.Karafarini.gov.ir).

Financial reporting of these firms is very essential for the government, banks, financial and credit institutions and legal agencies. As Berger and Udell (1998) declare, the financial institutions and commercial banks are the main creditors of the small firms (Berger & Udell, 1998). It should be mentioned that the separation of ownership and audit management made the social role become more important (Beshkooh et al, 2013). Additionally, different parts of the society mostly use audit services when the role of auditor becomes clear in the society (Abdollahi, 2012). Recently, there has been a provision enacted by the economic commission of the government in which it is mentioned that the audited financial statements are valid. In this enacted provision, granting a bank credit and assignment of the currency to the individuals without the audited financial statements is not allowed. Additionally, the executive regulation of the fourth note of the regulation of Iran certified public accountants of Iran regards that those firms with a specific level of revenue higher than a specified level, should prepare audited financial statements. There is no comprehensive study conducted about the audit problems of small business firms and there are no published journals in which some aspects had been temporarily studied; therefore, the present paper aims to investigate and identify the defined problems and rank these problems based on the significance degree from the point of view of the auditors.

2-LITERATURE REVIEW

Keasey et al (1988) primarily examined the audit terms of small firms and selected a sample composed of 540 reports of small firms which had been audited by big audit firms. The financial, organizational and audit variables

were tested by using significant empirical findings and multi-dimensions analyses. They found that those firms which have high levels of loans, more audit lag or few numbers of nonexecutive shareholders of the prior year, are more possible to be audited by the other firms.

Carey et al (2000) tried to examine the discretionary demand of the family firms for internal and independent audit. They initially studied the impact of normal specifications of the companies on the cost-benefit of employing the auditor and then tested whether the internal auditor remains as the amplifier of the costs of the independent auditor or it just works as an alternative monitoring mechanism. After describing the discretionary demand of auditing from 186 family corporations, they found that internal audit is more common than the independent audit. The significant correlation has also been confirmed. They could show that the internal audit works as a supplement rather than an alternative monitoring mechanism for the independent auditor. Using Lyzra model, the impact of agency cost on the demand of the independent audit was proved.

Iwisi et al (2002) conducted a study concerning the relationship of auditing small firms and explored the problems of the auditors in the selected countries of South African Development Association (SADC) and believed that regardless of the problems of auditing the small firms, the opportunity for growth and development would increase. This study indicates that the characteristics of the small firms of these three firms of SADC are similar to the characteristics of the small firms in other same countries .

Collis et al (2004) investigated the demand of auditing in small firms of Britain and examined whether the three measures of return, balance sheet and the number of employees could be suitable for the size of the small firms asking for auditing. They found that the return can demonstrate the firm size, but from the point of view of the managers, the firm size is less important .

Pumphrey and Trimmer (2005) use the opinions of three independent auditors of small firms which apply the organizational systems of those firms and found that none of the firms have formal politics for auditing these environments .

Collis et al (2008) explored the vision of the managers about auditing and accounting which is required for the small and medium firms. The results disclosed that the significant ratio of the managers believe that there are benefits in following the regulations of big firms. Additionally, they concluded that simplifying without a change in the description of the regulations might not contribute the small firms .

Salleh (2011) investigated the problems of auditing the small Malaysian firms. His finding confirmed the results of the study conducted by Riborn and colleagues in 1983. However, Riborn et al (1983) declare that the audit problems of small firms can be classified in terms of two groups: economic problems with which the auditors are involved in auditing the small firms than the bigger ones; and the deficiencies arising from the weaknesses of internal control system. Salleh (2011) also confirms the results through his study.

Chan (2012) studied whether the audit firms remain when they conduct the discretionary auditing. He tried to investigate the annual auditing exemption of small firms. He found that the audit clients tend to continue their audit if it would provide quality for them; even if the audit becomes a voluntarily process for the small firms.

3-METHODOLOGY

The present paper is an applied study using descriptive-survey method. Any scientific research seeks to find an answer to the questions or prove the hypotheses in this field. This study designs some questions about the research which include:

The first question: what are the main audit problems of the small firms from the point of view of the certified public accountants?

The second question: what is the priority level of these problems from their perspective?

4-POPULATION AND SAMPLE

The first step in a field study is the determination of the statistical population. Defining the population and the research nature might help the researcher to select a proper method for sampling. The population of this study is composed of the certified public accountants (the individual employee's member, the partner employee's member, the employee of the audit firms and the employee of the member institutions) and this comes to 1351 individuals. Based on the nature of the population and the random sampling method, the sample members have been identified. In this step, the confidence level is 95 percent and the ratio is included for the largest size of 0.5 and the acceptable error of the population has been regarded at 0.1 level.

$$n_0 = \frac{(z_{\alpha})^2 p(1-p)}{d^2}$$

$$n = \frac{n_0 N}{n_0 + (N-1)}$$

$$n_0 = \frac{(1/96)^2 * .5 * .5}{(0/1)^2} = 96$$

$$n = \frac{96 * 1351}{96 + (1351-1)} \cong 89.7$$

Z: is the quantile of normal distribution= 1.96 (for the confidence level of 95 percent)

P: is the ratio of the responses (0.5 at the worst situation)

N: the volume of the population

N0: the volume of the first sample

n: the modified sample based on the volume of the population

At the first step and according to the prior experiences and the prediction of the low rate of return, 110 questionnaires were distributed among the target population selected by using simple random method. The return rate of the questionnaire was not sufficient. Therefore, 30 questionnaires were again distributed and the completed questionnaires had been analyzed.

Among the distributed questionnaires, 96 ones were returned and six of them were not complete and could not be investigated. Thus 90 questionnaires were finally confirmed.

5-DATA COLLECTION

Initially, some of the certified public accountants were interviewed to identify the main problems of auditing the small firms of Iran. This affair was accompanied by reviewing the expert journals and books and empirical investigation. Subsequently, the primary schedule of the problems was prepared and classified into two general categories of internal and external. The subgroups of these aspects are indicated in table1.

According to the provided schedule, a questionnaire composed of two general sections has been modified. The first section includes the personal information (demographic characteristics) of the respondents and the second section involves the questions that concern identifying and ranking the auditing problems of the small firms. The validity of the questionnaire has been tested by sending the questionnaire to a group of the certified public accountants. Considering their corrections and comments, the questions were limited to 27 questions. The reliability of this questionnaire was measured by using Chronbach's alpha (0.87, and reliable enough). After making sure of the reliability and validity of the questionnaire, it has been distributed among the population. The final classification of the questionnaire is based on the following table:

Table1. Classifying the Questions in Main and Secondary Groups

	External			Internal	
	Accounting and Auditing Standards	Legal	Organizational Structure	Human Resource	Managerial
Question Number	4-18-20-23-26	5-9-13	1-7-8-11-12-14-17	6-10-25	2-3-15-16-19-21-22-24-27

6-TECHNIQUES FOR DATA ANALYSIS

After collecting the completed questionnaires, the qualitative measures were converted into quantitative ones by applying five-point Likert scale (5=very much and 1= very little). As the first stage, the information of the questionnaire was investigated from the point of view of the respondents as a whole and particularly. After that, these problems are ranked by statistical methods. These methods are as follows:

- *One Sample t-test:* This method is used when the mean of a given amount is intended to be compared. This test is utilized to test the 27 problems. In doing so, the mean of the responses of each question is compared with 3 and the larger number is the item considered by the respondents as important.
- *Two Independent Samples t-test:* This test is applied when the comparison of the mean of the two independent populations is regarded. In this section, based on the few numbers of the samples in some of the subgroups, non-parametric tests are utilized. In this project, the impact of binary demographic factors is examined by Mann-Whitney test.
- *K Independent Samples t-test:* This method is the most appropriate when the means of more than two populations are compared. In this study, the impact of the factors like age, education, major on the responses of this test has been tested. Non-parametric test of this section is Kruskal-Wallis.

- *Paired Samples t-test*: This test compares the mean of the two dependent populations. The present paper applies this test to compare the significance of the problems.
- *Mann-Whitney Test*: When there are two independent samples taken from a population and the variables are compounded; also when the terms of the parametric tests are not present in the variables or when the variables are not normal this test is applied, this test is used.
- *Kruskal- Wallis Test*: This is the test used for the comparison of the means of two ranked samples. The hypotheses of this test are unbiased and merely disclose the difference. It doesn't show the level of the groups in terms of their means.
- *TOPSIS Technique*: TOPSIS algorithm is a strong multiple criteria decision making technique for prioritizing the choices by simulating to the ideal solution. It has low sensitivity to the weighting technique and the responses have no deep variations. In this method, the selected choice is the one which has the shortest distance from the ideal solution.
- *Cluster Analysis*: This type of analysis is designed for a problem in which the observations (individuals) are classified in classes (clusters) with a sample of n observation and p variable on each variable. The same individuals are placed in one class. For doing cluster analysis, the average score of each variable is first computed as the input of the model and the 27 questions are classified in five clusters by using K mean method.

7-FINDINGS

- *The first main question*: what are the problems of the small audit firms?

Using single mean of independent sample, the average scores of any of the problems are compared with 3 and the findings are provided in table 2.

Table2. Examining the Position of the 27 Problems

Question Number	Audit Problems	Average Score	t	Sig
9	Audit requisitions just for the mandatory necessities not for their needs	4.07	12.366	.000
24	Abnormal requisitions and illogical expectations from the auditors' auditors	3.97	11.469	.000
23	Misapprehension of the managers in relation to the real audit fees and their efforts to irrational reduction	3.92	10.444	.000
1	Weakness of the internal control system	3.88	7.502	.000
22	Incomprehension of the transparent information and reservation of the information	3.84	8.796	.000
19	Misapprehension of the managers and firms from the aims and contents of audit and the auditing report	3.84	9.612	.000
3	Lack of information of the managers about their tasks in relation to the firm and accounting department particularly	3.80	9.213	.000
4	Failure to follow any separate entity assumption	3.74	6.904	.000
21	Facility in changing the auditors of the small firms because of the owners' managers	3.74	6.904	.000
11	Lack of a given organizational chart in a firm and the problems concerning separation of duties	3.72	7.723	.000
6	Lack of experienced personnel in accounting department	3.71	9.334	.000
16	The relation-oriented selection of the inspectors and non-familiarity of them with their tasks	3.71	7.805	.000
27	Sensitivity of the small firms on the audit results	3.70	7.239	.000
8	Firms' weakness in preparing financial statements	3.69	7.202	.000
15	Less financial and social knowledge of the small firms' directors in relation to the big firms	3.64	7.408	.000
20	High audit risk in small firms	3.61	5.091	.000
26	Limited time and budget of audit and less benefits in auditing the small firms	3.57	6.335	.000
14	Lack of financial advisors for management in comparison with the big firms	3.51	5.230	.000
13	Non formation of the conventions and board of directors in the appointed and legal time and non-establishment of the proceeding	3.49	4.760	.000
2	Lack of economic justification of auditing in terms of the firms	3.48	5.168	.000
25	Dissatisfaction of the accounting personnel from the auditors and fear from losing their position	3.43	5.088	.000
12	Non establishment of the audit committees in small firms	3.41	2.893	.005
10	Disproportion of the number of accounting personnel in relation to the volume of the operations of the firm	3.39	4.178	.000
18	Impossibility of implementing risk based auditing (content audit frequently)	3.28	2.116	.037
5	The lack of rules, regulations and standards of small firms	3.22	2.351	.021
7	The weakness of accounting structure of these firms including the lack of legal books and proper mechanized system	3.19	1.765	.081
17	Limited buyers, vendors and other parties of the contractors in small firms	3.14	1.754	.089

According to the significant level of t statistics of the questions, all problems are considered significant except for items 7 and 17 at the level of 95 percent. This is because the significance levels of all questions are lower than five. Items 7 and 17 are significant at 0.90 because their significance is lower than 10 percent. Generally, it can be concluded that all problems are taken into account as the significant problems associated with the auditing of the small Iranian firms.

Based on the significance of the problems in this study, the important problems of auditing small firms have been identified in Iran field.

➤ The second main question: What is the order of prioritization and pattern of ranking these problems? The table below shows the ranking of the problems by using TOPSIS method.

Table3. Ranking the Problems by Using TOPSIS method

Question Number	Question	Score	Rank
1	Weakness of the internal control system	13.31	1
12	Non establishment of the audit committees in small firms	13.10	2
18	Impossibility of implementing risk based auditing (content audit frequently)	12.83	3
20	High audit risk in small firms	12.50	4
7	The weakness of accounting structure of these firms including the lack of legal books and proper mechanized system	12.44	5
4	Failure to follow any separate entity assumption	12.27	6
17	Limited buyers, vendors and other parties of the contractors in small firms	11.85	7
21	Facility in changing the auditors of the small firms because of the owners' managers	11.80	8
27	Sensitivity of the small firms on the audit results	11.70	9
5	The lack of rules, regulations and standards of small firms	11.65	10
9	Audit requisitions just for the mandatory necessities not for their needs	11.56	11
2	Lack of economic justification of auditing in terms of the firms	11.18	12
13	Non formation of the conventions and board of directors in the appointed and legal time and non-establishment of the proceeding	11.06	13
22	Incomprehension of the transparent information and reservation of the information	10.85	14
8	Firms' weakness in preparing financial statements	10.80	15
11	Lack of a given organizational chart in a firm and the problems concerning separation of duties	10.71	16
25	Dissatisfaction of the accounting personnel from the auditors and fear from losing their position	10.65	17
24	Abnormal requisitions and illogical expectations from the auditors' auditors	10.63	18
26	Limited time and budget of audit and less benefits in auditing the small firms	10.62	19
3	Lack of information of the managers about their tasks in relation to the firm and accounting department particularly	10.46	20
10	Disproportion of the number of accounting personnel in relation to the volume of the operations of the firm	10.30	21
6	Lack of experienced personnel in accounting department	10.30	22
19	Misapprehension of the managers and firms from the aims and contents of audit and the auditing report	10.16	23
23	Misapprehension of the managers in relation to the real audit fees and their efforts to irrational reduction	10.09	24
14	Lack of financial advisors for management in comparison with the big firms	9.94	25
16	The relation-oriented selection of the inspectors and non-familiarity of them with their tasks	9.45	26
15	Less financial and social knowledge of the small firms' directors in relation to the big firms	9.45	27

Table 3 summarizes the ranking of any of the problems by using TOPSIS technique. As shown in table above, the respondents believe that the major problem is related to the weakness in the internal control system of the small firms. However, the item with the least importance is lack of financial and social knowledge of the managers of the small firms rather than the big firms. The rankings of the other problems are also provided in table above.

➤ Clustering the audit problems from the point of view of the whole population:

In this section, the cluster analysis has been used to determine the real position of the problems in terms of significance and from the respondents' perspective. Using this method, the questions are classified in five clusters. The findings are separately provided in table 4.

Table4. Clustering the Audit Problems from the Perspective of the Whole Population

Cluster Number	Cluster Center	Number of the Questions in a Cluster	Questions
1	4.07	2	Q9 Q24
2	3.84	5	Q1 Q3 Q19 Q22 Q23
3	3.64	10	Q4 Q6 Q8 Q11 Q15 Q16 Q2 Q21 Q26 Q27
4	3.41	6	Q2 Q10 Q12 Q13 Q14 Q15
5	3.14	4	Q5 Q7 Q17 Q18

It should be noted that cluster 1 contains the most important problems mentioned in questions 9 and 24. However, cluster 5 involves the problems with the least significance and the problems between them are shown in the order of their significance. It must be mentioned that the previous section (table 3) provided the problems by using TOPSIS technique, but table 4 ranks the problems by a statistical method. The difference is that the ranking of each question is identified by TOPSIS technique but in the clustering technique, those questions with the similar statistical significance are clustered in a same category.

➤ The other findings of this study are as below:

Two paired samples test is applied to examine the difference between the problems in the internal and external fields. The findings are provided in table 5.

Table5. The Difference of Significance between the two problems

	Paired Differences			t	Df	Sig
	Mean	Std. Deviation	Mean Error			
External- Internal	-.01033	.35428	.03734	-.277	89	.783

As shown in table above, the significance level of t statistics is greater than 5%. Therefore, it can be concluded that the difference between internal and external problems are rejected at 95 percent and these problems are considered by the respondents as the problems with the same significance.

In this section, the significance of the differences has been examined in five fields by using paired samples tests and the findings are provided in table 6.

Table6. Examining the Difference between Five Problems

	Paired Differences			t	Df	Sig
	Mean	St. Deviation	Mean Error			
Legal-organizational structure	.08624	.60238	.06350	1.358	89	.178
Legal- accounting and standards	.03704	.53863	.05678	.652	89	.516
Legal-human resource	.08148	.68934	.07266	1.121	89	.265
Legal- managerial	-.15556	.51007	.05377	-2.893	89	.005
Organizational structure- accounting and auditing standards	-.04921	.52006	.05482	-.898	89	.372
Organizational structure- human resource	-.00476	.62391	.06577	-.072	89	.942
Organizational structure- managerial	-.24180	.56992	.06007	-4.025	89	.000
Accounting and auditing standards- human resource	.04444	.67402	.07105	.626	89	.533
Accounting and auditing standards- managerial	-.19259	.47157	.04971	-3.875	89	.000
Human resource- managerial	-.23704	.59175	.06238	-3.800	89	.000

As shown in table above, the significance level of t statistics related to the comparison of managerial problems with the other problems are lower than five percent and t statistics of the comparison of other problems is greater than 5 percent. Therefore, it can be concluded that the managerial problems in comparison with the other problems have the highest importance and the other four schemes are considered to have the same significance.

➤ In addition, the impact of the demographic characteristics of the respondents on their opinions about the significance of the problems has been investigated and the results are as follows:

Table 7. The Impact of Demographic Characteristics of the Respondents on the Opinions about the Significance of the Problems

variable	position		legal	Organizational structure	Accounting and auditing standards	Human resource	Managerial	External	Internal
Gender	Male	Mann-Whitney U	358.500	196.500	295.500	366.000	395.500	312.000	334.500
	Female	Wilcoxon W	3518.500	3356.500	3455.500	432.000	3555.500	3472.000	3494.500
		Z	-.954	-2.944	-1.719	-.860	-.482	-1.514	-1.233
		Asymp. Sig. (2-tailed)	.340	.003	.086	.390	.630	.130	.217
Education	Ph.D	Chi-square	5.004	2.391	3.601	3.206	3.595	2.665	3.652
	Master	Df	3	3	3	3	3	3	3
	Bachelor	Asymp. Sig.	.172	.495	.308	.361	.309	.446	.302
Major	Accounting	Chi-square	.254	.707	2.746	1.135	.236	3.150	.177
	Management	Df	2	2	2	2	2	2	2
	Economics	Asymp. Sig.	.881	.702	.253	.567	.889	.207	.915
The main activity	Manager	Chi-square	1.874	1.028	3.703	1.002	2.215	3.477	.611
	Partner	Df	3	3	3	3	3	3	3
	Top supervisor	Asymp. Sig.	.599	.795	.295	.801	.529	.324	.894
	Other								
Duration of the operation	5>	Chi-square	11.052	4.845	8.295	7.936	8.344	10.179	5.548
	6-10	Df	5	5	5	5	5	5	5
	11-15	Asymp. Sig.	.050	.435	.141	.160	.138	.070	.353
	16-20								
	21-25								
Age	25<								
	35>	Chi-square	5.179	3.361	8.666	.896	4.003	8.876	2.110
	36-45	Df	3	3	3	3	3	3	3
	46-55	Asymp. Sig.	.159	.339	.034	.826	.261	.031	.550
Training background	55<								
	none	Chi-square	7.083	7.446	6.675	8.073	3.828	8.892	8.896
	1-5	Df	4	4	4	4	4	4	4
	6-10	Asymp. Sig.	.132	.114	.154	.089	.430	.064	.064
	11-15								
	15<								

According to the investigations, it was found that gender specification merely influences on the opinions of the respondents about the significance of the problems related to the organizational structure, so that the females consider the organizational structure more important.

The impact of duration of the operations by the respondents has been identified at the significance level of 90 percent which influences on the opinions of the respondents about the legal and external problems. Consequently, those individuals with lower working background consider the legal and external problems more essential.

The findings also reveal that the education level, major and the main operations of the respondents have no impact on the problems from their perspective.

It was identified that the respondents' age has no influence on the opinions of the respondents about the significance level of the problems of auditing and accounting standards and external problems. Therefore, those individuals who are older than the others consider the problems of auditing and accounting more important.

In terms of the impact of training experience duration on the opinions of the respondents, it was identified that the level of training experience influences on the opinions of the respondents about the significance level of the human resources and external and internal problems at the 90 percent level of significance. Those individuals who have more training experiences consider the human resources, external and internal problems more important.

8-CONCLUSIONS AND SUGGESTIONS

The findings of this study demonstrated that the members of the target population, who are among the custodians of the profession, consider these 27 problems essential and this is a warning for the profession and small firms. To maintain or enhance the profession, the executives and the custodians should pay special attention to these problems and endeavor to identify the causes and solve these problems as soon as possible.

According to the findings, the suggestions are classified into two categories:

★ Findings- based suggestions

- Weakness of internal control systems in small firms is one of the most significant problems of auditing in such firms and it makes the managers to increase their efforts in evaluating the performance of the internal control

system. In addition, the auditors should also pay attention to this subject in determining the risk level of the small firms.

- Another crucial subject in auditing the small firms is the laws and regulations specially designed for the small firms which require the professional accounting agencies to take this into account and select the best choices to solve this problem.
- The managers of the small firms and those who audit these firms are also offered to take into account the specific problems and try to overcome them.

★Further Studies Suggestions

- The future studies could be devoted to examining the problems of auditing the small firms from the point of view of the directors to provide a chance to perceive the results and offer corrective opinions.
- Another interesting subject might be investigating the required approaches to solve the deficiencies of the study.
- The central point of this study has a general nature. Therefore, it is suggested to examine the identified elements in detail. For example, reliance or non-reliance on the internal controls can be tested in various future studies.
- The way to complete the internal controls of the small firms can be studied from the directors' perspective.
- The issue related to the efficiency of auditing the small firms is a base for the further study.
- Auditing small firms through a modern method might be considered as a title to be further examined.

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